United States Court of Appeals

for the Second Circuit

REPLY BRIEF

Signed

76-4062

IN THE UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

POIRIER & MCLANE CORPORATION,

Appellee

v.

COMMISSIONER OF INTERNAL REVENUE,

Appellant

B
P/S

ON APPEAL FROM THE DECISION OF THE UNITED STATES TAX COURT

REPLY BRIEF FOR THE APPELLANT

SCOTT P. CRAMPTON,
Assistant Attorney General,

GILBERT E. ANDREWS,
ROBERT A. BERNSTEIN,
JOHN G. MANNING,
Attorneys,
Tax Division,
Department of Justice,
Washington, D.C. 20530.

IN THE UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 76-4062

POIRIER & MCLANE CORPORATION,

Appellee

v.

COMMISSIONER OF INTERNAL REVENUE,

Appellant

ON APPEAL FROM THE DECISION OF THE UNITED STATES TAX COURT

REPLY BRIEF FOR THE APPELLANT

This reply brief is addressed only to those points raised in the taxpayer's brief that we believe to require further discussion, and it is not intended to restate the arguments in our opening brief.

In its brief taxpayer asserts at several places (Br. 6, 15-16, 17-18, 20, 22) that the transfer of $1,100,000 to the Manufacturers Hanover Trust Company for the purpose of satisfying the contested damage claims against it created a valid trust under New York law of which the claimants were the intended beneficiaries. We do not dispute that, as found by both the Tax Court majority and the dissent (R. 59, 66), a valid trust was created.

However, taxpayer's assertion that the claimants were the intended beneficiaries of the trust assumes the answer to one of the principal questions at issue here, _viz._, whether taxpayer, rather than the claimants, was the intended beneficiary of the trust.

Indeed, taxpayer does not even address the argument in our opening brief (pp. 12-13, 17) that the claimants were not the beneficiaries of the trust because, under settled principles of trust law, the grantor is presumed to be the beneficiary of a trust established for the payment of a creditor who has not agreed to the trust's creation. Nor does taxpayer dispute the proposition (_ibid._) that, if taxpayer was the sole beneficiary of the trust, he had the right to revoke the trust at any time and that taxpayer therefore did not transfer the fund "beyond his control," as required by the Treasury Regulation [1/] in accordance with the legislative history [2/] of Section 461(f) of the Internal Revenue Code. Accordingly, taxpayer's argument is, in large part, unresponsive and irrelevant.

1/ Treasury Regulations on Income Tax (1954 Code), §1.461-2(c).

2/ S. Rep. No. 830, Part 2, 88th Cong., 2d Sess., p. 243 (1964-1 Cum. Bull. (Part 2) 700, 746).

That the transferred funds were not placed beyond taxpayer's control (nor delivered in accordance with the settlement of the contest over the claims, as required by the Treasury Regulation),[3/] is demonstrated also (see pp. 19-21 of our opening brief) by the fact that, contrary to taxpayer's assertion (Br. 4, 16), all of the claims were not disposed of when the trust was revoked and its corpus was returned to taxpayer in November, 1969. To be sure, taxpayer's management may have reasonably believed at the time that the amount of the claims, as finally determined, would be well within taxpayer's maximum insurance coverage for negligence; further, the trustee, as taxpayer suggests (Br. 23-24), may have acted properly in returning the fund to taxpayer. However, the very fact that taxpayer requested the return of the fund, and that the trustee acceded to this request, before the claims were finally determined shows that the $1,100,000 transferred into trust was not unconditionally dedicated to the payment of the claims. Rather, the fund was merely set aside until such time as the liability of taxpayer's insurance carrier became certain or reasonably so. In effect, taxpayer claims a deduction for funds set aside for the satisfaction of the claims, but later withdrawn in reliance on the obligation of another

3/ Treasury Regulations on Income Tax (1954 Code), § 1.461-2(c).

party (the insurer) to pay the claims. Accordingly, taxpayer's claim is contrary to the legislative intent,[4/] as reflected in the Treasury Regulation,[5/] that a taxpayer who merely procures a guarantee from another person of payment of a contested claim, (e.g., by purchasing a bondsman's bond) does not qualify for the deduction.

Taxpayer also argues (Br. 13-14) that the requirement of the Treasury Regulation that a claimant be a party to the trust or escrow would allow the claimants in the instant case to deprive taxpayer of the deduction by arbitrarily refusing to sign the trust instrument. The simple answer is that no reasonable claimant would act against his own interest by refusing to sign an instrument that establishes a fund for the payment of his claim. The Tax Court suggested, however, that a claimant might be reluctant to sign the trust instrument for fear of "thereby implicitly * * * limiting * * * [his] claim at the outset of the litigiation to the entrusted amount" (R. 57, fn. 9). But any such potential problem could be easily avoided by a provision in the agreement that a claimant's participation therein should not be construed as a limitation on the amount of his recovery. Accordingly, the requirement of the Treasury Regulation that a claimant be a party to an agreement under

4/ S. Rep. No. 830, Part 2, 88th Cong., 2d Sess., p. 243 (1964-1 Cum. Bull. (Part 2) 700, 746).

5/ Treasury Regulations on Income Tax (1954 Code), §1.461-2(c).

which funds are transferred for the purpose of satisfying his claim does not, in any realistic sense, make taxpayer's ability to qualify for a deduction under Section 461(f) dependent upon the whims of the claimants here.

Respectfully submitted,

SCOTT P. CRAMPTON,
Assistant Attorney General,

GILBERT E. ANDREWS,
ROBERT A. BERNSTEIN,
JOHN G. MANNING,
Attorneys,
Tax Division,
Department of Justice,
Washington, D.C. 20530.

JUNE, 1976.

CERTIFICATE OF SERVICE

It is hereby certified that service of this reply brief has been made on opposing counsel by mailing four copies thereof on this 21st day of June, 1976, in an envelope, with postage prepaid, properly addressed to them as follows:

Edward S. St.John, Esquire
Thomas P. Dougherty, Esquire
St.John & Dougherty
The Colonial Office Building
14 Vanderventer Avenue
Port Washington, New York 11050

Gilbert E. Andrews / [illegible]
GILBERT E. ANDREWS,
Attorney.